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SUBJECT: MAINTAINING MCC MOMENTUM IN PARAGUAY

SUMMARY

11. (U) US Embassy Asuncion Country Team endorses Ambassador Danilovich's recommendation to the MCC Board that Paraguay be considered for a proposed Stage II MCC Threshold Program. Our support is based on progress made under Paraguay's current Threshold program, its empirical advances on the MCC Performance Scorecard, and our view that both the Threshold program and the future prospect of a MCC Compact are powerful medicine in a country that is both seeking to reform and modernize, and is markedly open to US partnership. With national elections taking place in April 2008, a Stage II Threshold Program would present a vital opportunity for both the USG and a new Government of Paraguay (GOP) to directly address mutual interests and key constraints that continue to hamper Paraguay's development and democratic consolidation, as well as enhance long-term regional security.

Progress on the Threshold

12. (U) Approved in 2006 as Latin America's first Threshold program, Paraguay's MCC effort (known locally as "Programa Umbral") is a highly ambitious anti-corruption initiative directed at reducing rampant impunity and economic informality. Halfway through its life (the bilateral grant agreement expires in November 2008), Paraguay has demonstrated tangible progress in addressing its systemic corruption. In one of the most salient examples of how the MCC program has helped promote economic formalization, Paraguay has significantly streamlined its business registration process, slicing costs and time to the entrepreneur, and leapt over 72 countries in the latest Doing Business survey. The Threshold program also assisted the GOP in taking the unpopular but necessary steps to identify and suspend temporarily businesses that have been evading taxes. More than 30 companies have been suspended via judicial order to date. GOP follow-through on the suspensions appears to be changing behavior; based on the Tax Ministry's initial analysis, collections of value-added taxes of surveyed businesses have increased by an average of 21 percent.

13. (U) The program has catalyzed unprecedented inter-institutional cooperation among the 28 public ministries and branches of government that participate in and benefit from the Threshold Program. These include forcing coordination among seven ministries and the judiciary to simplify business registration; the first-ever protocol between the Public Ministry and Customs on how to handle contraband seizures for evidence in prosecution; and, improved services resulting from integration of effort between ministries that manage separate public registries.

14. (U) With MCC assistance, nearly USD 5 million has been seized in contraband by specialized units. These results reflect the GOP's desire to formalize economic activity in the country. As part of its Threshold commitments, the Supreme Court developed and approved a series of comprehensive internal reform measures that include new methods for improving efficiency, increasing transparency, and ultimately holding judges accountable for their actions. Finally, two specialized units supported by MCC have developed and investigated nearly 300 suspected incidents of internal government malfeasance or corruption resulting in 80 cases submitted to the Attorney General's office for further investigation and possible prosecution.

15. (U) Paraguay has also made appreciable gains on its position on the MCA Performance Scorecard. Paraguay is "green," or above the median in comparison with 95 other countries, on 13 of 17 policy indicators. On many of these indicators, Paraguay ranks in the 80 or 90th percentiles. Paraguay's advances are particularly significant in Economic Freedom, due to its solid macro-economic management and Threshold-supported business climate improvements, which are reflected in Paraguay moving fully to green on all six indicators in this category. On the high hurdle of "Control of Corruption," Paraguay has also progressed steadily, moving from its 8th percentile place in FY2005, to its current position of 30th. While Paraguay still has much work to do and many challenges remaining to get above the mean on Control of Corruption, in effect their lone MCC Compact deal-breaker, it is clear that they are moving in a positive direction. The Threshold Program has provided clear leverage for those many Paraguayans actively working to combat corruption.

What's Next?

16. (U) The MCC discussions about possible Stage II Threshold assistance for countries that have performed well but are not yet eligible for MCC Compacts will be critically important to Paraguay, and central to our ability to pursue and attain our highest priority foreign policy and development goals: democratic consolidation and regional security.

17. (U) The MCC Threshold Program, and the question of what's next for Paraguay if not a Compact, become all the more important as we consider that Paraguay will hold national elections for President, Vice President, governors and all members of Congress in April 2008, and a new government will take power in August. The current Threshold Program for Paraguay ends in November 2008; however, many of the activities will be finished by June 2008. Stage II Threshold assistance will be vital to consolidate gains being made under the program now and to pave the way for continued reform by the next

administration. The timing is such that a Stage II Threshold program would play a pivotal role in the USG's ability to constructively engage and assist the new government with its reform and development agenda.

18. (U) While a Stage II Threshold program should be shaped by the priorities of whichever candidate or party wins the April elections, Threshold II should address the major fault lines that continue to affect Paraguay's score on the Corruption Control indicator. Based on the in-depth MCC indicator analysis of Paraguay's Control of Corruption that MCC prepared and provided to the GOP earlier this year, a Threshold Stage II program could have considerable impact by tackling key corruption issues that are not a direct part of our current Threshold I assistance. These include items such as, greater reforms of the criminal justice system (including criminal procedure code improvements), ensuring non-political selection of judges, and promoting better access to information (FOIA reform). Paraguay's waning competitiveness and economic prosperity prospects would also be substantially boosted by attention to additional business policy climate improvements. Threshold Stage II could also have significant impact with assistance to solidify and deepen the adoption of a few select Threshold I objectives that will likely require more time to take hold, such as strengthening anti-corruption prosecution capacity, improving GOP budget transparency/internal controls, and strengthened customs enforcement capabilities.

19. COMMENT: The MCC Threshold program and the promise of a future Compact have provided significant leverage and incentive for Paraguay to modernize and reform. Post firmly believes that Paraguay's performance and policy progress provide a persuasive case for a Stage II MCC Threshold. Paraguay's path has been lit in part with support from the MCC Threshold Program. The torch will be passed to a new administration with new priorities and a new agenda next few months. Continued MCC Threshold assistance will be a critical part of our ability to help the new administration keep the torch lit, and leading down a path to democratic consolidation and broader-based prosperity for Paraguayans. END COMMENT

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